Supreme Court, U.S.
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No. _____

In The

Supreme Court of the United States

FARM CREDIT SERVICES OF MID-AMERICA, ACA,

Petitioner,

v.

THOMAS M. ZAINO,
Tax Commissioner of Ohio,

Respondent.

On Petition For A Writ Of Certiorari To The Supreme Court Of Ohio

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Agricultural Credit Associations are member institutions of the Farm Credit System, formed by the merger of Federal Land Bank Associations (which make long-term real estate mortgage loans to agricultural borrowers) and Production Credit Associations (which make short- and intermediate-term operating loans to agricultural borrowers.) Congress provided that Agricultural Credit Associations "shall possess all powers granted under [the Farm Credit Act] to" and "shall be subject to all of the obligations imposed under [the Farm Credit Act] on" their predecessor associations. 12 U.S.C. § 2279c-1(b)(1). The Farm Credit Act expressly prohibits the states from taxing the income of Federal Land Bank Associations. 12 U.S.C. § 2098.

The question presented is whether Congress has authorized states to tax the income of Agricultural Credit Associations from long-term real estate mortgage lending, when states were prohibited from taxing the income of the predecessor Federal Land Bank Associations from the same lending activity.

PARTIES TO THE PROCEEDINGS BELOW

The parties to the proceedings below were Farm Credit Services of Mid-America, ACA, and Roger W. Tracy, the then Tax Commissioner of Ohio, in his representative capacity. Mr. Tracy was succeeded by Thomas M. Zaino, the current Tax Commissioner of Ohio, in his representative capacity.

Pursuant to Supreme Court Rule 29.6, no publicly held company owns 10% or more of the stock of Farm Credit Services of Mid-America, ACA.

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DECISIONS BELOW

The decision of the Ohio Supreme Court (Pet. App. 1-7) is reported at 747 N.E.2d 814 (Ohio 2001). The decision of the Ohio Board of Tax Appeals (Pet. App. 8-12) is not reported.

JURISDICTION

The judgment of the Ohio Supreme Court was entered on June 6, 2001. This Court's jurisdiction rests on 28 U.S.C. § 1257(a).

STATUTES INVOLVED

The relevant provisions of the Farm Credit Act, 12 U.S.C. §§ 2077, 2098, and 2279c-1, are set forth at Pet. App. 13-15.

STATEMENT OF THE CASE

Agricultural Credit Associations

Farm Credit Services of Mid-America, ACA ("Mid-America") is an Agricultural Credit Association and a member institution of the Farm Credit System. 12 U.S.C. § 2001 *et seq.* Mid-America is a "federally chartered instrumentality" of the United States, authorized to provide agricultural credit in Ohio, Indiana, Kentucky and Tennessee. There are more than sixty Agricultural Credit Associations authorized to provide agricultural credit in

all fifty states. Agricultural Credit Associations constitute the single largest class of lending institutions in the Farm Credit System. Farm Credit Administration Accountability Report Fiscal Year 2000.

Congress authorized the formation of Agricultural Credit Associations in the Agricultural Credit Act of 1987, Pub. L. 100-233, 101 Stat. 1568 (the "1987 Act"). The 1987 Act was enacted in response to depression conditions in the agricultural economy that threatened the viability of the Farm Credit System. The House Committee Report on P.L. 100-233 described the circumstances facing the Farm Credit System:

> The Farm Credit System has suffered massive losses, $2.7 billion in 1985 and $1.9 billion in 1986, with losses continuing into 1987 at an apparently lower rate, thereby posting a loss of $201 million through June 30, 1987. Projections for future losses by the System's Farm Credit Corporation of America show expected losses of $1.282 billion for 1987, $1.090 billion for 1988 and $742 million for 1989. The System's combined surplus is forecast to be $121 million in 1987, a deficit of $1.026 billion in 1988 and a deficit of $1.826 billion in 1989.

H.R. Rep. No. 295, 100th Cong. 1st Sess. at 57 (1987). One consequence of these losses was an increase in the interest rates charged to the System's borrowers. The Senate Committee Report explained:

> During periods of depressed commodity prices and falling farm land values, farmers need, more than ever, access to reasonably priced credit. Yet, pressures on all farm lenders to offset losses has too often pushed up interest rates

> to farmers and merely accelerated their financial difficulties.

S. Rep. No. 230, 100th Cong. 1st Sess. at 21 (1987).

In response to the agricultural crisis, Congress authorized $4 billion of federal assistance, 12 U.S.C. § 2278b-6, and also authorized a large scale restructuring of the Farm Credit System. The goal was to shore up the System's finances and reduce its costs, thus permitting lower interest rates on loans to the System's borrowers. S. Rep. No. 230, 100th Cong. 1st Sess. at 21 (1987). One part of the restructuring program involved the creation of the Agricultural Credit Associations.

Section 411 of the 1987 Act required Federal Land Bank Associations and Production Credit Associations serving substantially similar territories to submit a plan of merger to their members. Pub. L. 100-233 § 411, 101 Stat. 1638. If the plan was approved, Section 416 of the Act authorized the associations to merge to form an Agricultural Credit Association. Pub. L. 100-233 § 416, 101 Stat. 1647-48 (now codified at 12 U.S.C. § 2279c-1). The goal of these mergers was to streamline the Farm Credit System, reduce costs, increase efficiency and assist member institutions in providing competitive interest rates to their member borrowers. 133 Cong.Rec.H 4988 (statement of Rep. Stallings), 133 Cong.Rec.S. 18458 (statement of Sen. Leahy).

The Federal Land Bank Associations and Production Credit Associations that merged to form Agricultural Credit Associations are authorized to provide different types of agricultural credit to their member borrowers. The Federal Land Bank Associations, which are governed

by 12 U.S.C. §§ 2091-2098, provide long-term real estate mortgage loans. Section 2098 provides that the income of the Federal Land Bank Associations, and the notes and obligations issued by the associations, are exempt from state income tax.

The Production Credit Associations, which are governed by 12 U.S.C. §§ 2071-2077, provide short- and intermediate-term operating loans. Section 2077 provides that the notes and other obligations issued by the Production Credit Associations are exempt from state income tax.

The Farm Credit Act provides that Agricultural Credit Associations shall have all powers and be subject to all of the obligations of their predecessor associations:

> Except as otherwise provided by this subchapter, a merged association shall –
>
> (A) possess all powers granted under this chapter [the Farm Credit Act] to the associations forming the merged association; and
>
> (B) be subject to all of the obligations imposed under this chapter [the Farm Credit Act] on the associations forming the merged association.

12 U.S.C. § 2279c-1(b)(1). Congress did not otherwise delineate the powers and obligations of Agricultural Credit Associations. Pursuant to 12 U.S.C. § 2279c-1, Agricultural Credit Associations now make both the long-term real estate mortgage loans and the short- and

intermediate-term operating loans previously made by their predecessor associations.[1]

Proceedings Below

Mid-America initially paid state income tax in Indiana, Ohio, Kentucky and Tennessee. Beginning in 1993, Mid-America filed refund claims to recover these taxes.[2] The Indiana Supreme Court concluded that Mid-America was exempt from Indiana state taxation on the income from its long-term real estate mortgage lending previously carried out by its Federal Land Bank Association predecessors but taxable on the income from its short- and intermediate-term lending previously carried on by its Production Credit Association predecessors. *Indiana Department of State Revenue v. Farm Credit Services of Mid-America, ACA*, 734 N.E.2d 551 (Ind. 2000) (reproduced at Pet. App. 16-42.)

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[1] Beginning in 1999, the Farm Credit Administration authorized Agricultural Credit Associations to set up two wholly owned subsidiaries to carry out their long-term real estate mortgage lending and short- and intermediate-term lending. A number of the Agricultural Credit Associations, including Mid-America, have converted to this structure. See generally Farm Credit Administration Accountability Report Fiscal Year 2000.

[2] The Tennessee Department of Revenue granted Mid-America's refunds. Mid-America's Kentucky claims are still pending. Other Agricultural Credit Associations also filed refund claims to recover the state taxes paid on their income from long-term real estate mortgage loans. While a number of states have granted refunds, claims are still pending in eleven states.

In Ohio, Mid-America's refund claims were initially denied by the Ohio Tax Commissioner and Mid-America appealed to the Ohio Board of Tax Appeals. Mid-America argued that it was a federal instrumentality and exempt from Ohio income tax because the relevant provisions of the Farm Credit Act did not authorize Ohio to tax. The Tax Commissioner responded that Mid-America was subject to Ohio income tax unless Congress provided a statutory exemption and that Congress had not done so. The Ohio Board of Tax Appeals held that Mid-America's claim of exemption involved a constitutional issue that the Board was not authorized to address. Pet. App. 12. As a result, the Ohio Board of Tax Appeals affirmed the Ohio Tax Commissioner's refund denials. Pet. App. 12.

Mid-America appealed to the Ohio Supreme Court. Mid-America renewed its claim that it is a federal instrumentality and exempt from state taxation absent congressional authorization. Mid-America also explained that Congress had statutorily exempted Agricultural Credit Associations from state taxation by providing in 12 U.S.C. § 2279c-1, that they succeeded to the state tax exemptions of their predecessor Federal Land Bank Associations and Production Credit Associations.

The Tax Commissioner cross-appealed, arguing that the Board should have addressed and decided the Tax Commissioner's claim that Congress had not conferred statutory immunity on Agricultural Credit Associations. The Tax Commissioner also argued that the Ohio Supreme Court should not decide whether Mid-America succeeded to the statutory tax exemptions of its predecessor associations pursuant to 12 U.S.C. § 2279c-1

because Mid-America had not affirmatively made that argument below.

The Ohio Supreme Court rejected Mid-America's claim of exemption from Ohio income tax as a federal instrumentality. The Ohio Supreme Court also, despite the Tax Commissioner's objection, directly addressed Mid-America's claim of statutory immunity under 12 U.S.C. § 2279c-1. The Ohio Supreme Court stated:

> We also dismiss Farm Credit Services' argument that language in the statute, asserting that merged associations possess all powers and assume all obligations of the merging associations, passes tax immunity to the successor association. According to normal usage, "powers" refers to the activities and actions the predecessor entities may undertake, and "obligations" refers to the debts, contractually and otherwise acquired duties that the predecessor entities have undertaken. Black's Law Dictionary (7 Ed.Rev. 1999) 1189-1190, 1102-1103.

Pet. App. 6. Mid-America challenges only that part of the Ohio Supreme Court's decision which holds that Mid-America is subject to Ohio income tax on its income from long-term real estate mortgage lending.

REASONS FOR GRANTING THE PETITION

This case presents an important and recurring federal question regarding state taxation of Agricultural Credit Associations, the largest class of lending institutions in the Farm Credit System. Two state Supreme Courts have issued directly conflicting decisions on this question. The

same issue is pending in eleven other states.[3] Certiorari should be granted to resolve the conflict and provide a definitive answer for Mid-America and the other associations and states facing this important question.

Certiorari should also be granted because the Ohio Supreme Court erred in concluding that Agricultural Credit Associations are taxable on the income from their long-term real estate mortgage loans. The structure of the Farm Credit Act, the text of Section 2279c-1 and Congress' seventy year old policy of prohibiting states from taxing income earned by Farm Credit System institutions on long-term real estate mortgage lending compel the conclusion that Ohio and other states may not tax Agricultural Credit Associations on this income.

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[3] Cases are pending before the Maryland Tax Court in *West Virginia Farm Credit, ACA et al. v. Comptroller of the Treasury*, No. 99-IN-OO-0292, the Michigan Court of Claims in *Farm Credit Services of East Central Michigan, ACA, et al. v. Michigan Department of Treasury*, 99-17210-CM, the Superior Court of Wake County, North Carolina in *Carolina Farm Credit, ACA, et al. v. North Carolina*, No. 00 CVS 11290, and the Oregon Tax Court in *Northwest Farm Credit Services, ACA v. Oregon Department of Revenue*, TCM No. 000903D. The remaining cases are pending before various state administrative tribunals in Kentucky, Montana, North Dakota, Virginia, Vermont, Washington and Wisconsin.

I. The Ohio Supreme Court Decision Conflicts With The Decision Of The Indiana Supreme Court On The Same Issue And Leaves Other Agricultural Credit Associations And States Uncertain About Taxation Of Agricultural Credit Associations

The Ohio Supreme Court's conclusion that Mid-America is subject to state income taxation on income from long-term real estate mortgage loans directly conflicts with the Indiana Supreme Court's decision on the same issue for the same taxpayer. In *Indiana Department of State Revenue v. Farm Credit Services of Mid-America, ACA,* 734 N.E.2d 551 (Ind. 2000), the Indiana Supreme Court held that Mid-America is not subject to Indiana's Financial Institutions Tax on its income from long-term real estate mortgage loans. 734 N.E.2d at 560. Pet. App. 37. The Court should grant this petition to resolve the conflict between the highest courts of Indiana and Ohio regarding the state taxation of Agricultural Credit Associations.

These conflicting decisions leave Agricultural Credit Associations and the states without clear guidance concerning the tax status of Agricultural Credit Associations. If some states tax ACAs and others do not, the lack of uniform treatment can create serious internal problems for those Agricultural Credit Associations that operate in more than one state. Disparate state taxation may force such associations to charge different interest rates to borrowers to compensate for the higher tax burden on long-term real estate mortgage loans in one state versus another. The Court should grant the petition and clarify the tax status of the Agricultural Credit Associations. This will avoid piecemeal litigation and uncertainty on a

question of financial and operational importance to a major segment of the Farm Credit System.

II. The Structure Of The Farm Credit Act, The Text Of 12 U.S.C. § 2279c-1 And Congress' Seventy Year Old Policy of Prohibiting States From Taxing The Income Of Farm Credit System Institutions Making Long-Term Real Estate Mortgage Loans Compel The Conclusion That Ohio Erred In Its Decision Below

The Farm Credit System consists of a number of federal institutions, each of which is specifically authorized by Congress and chartered by the Farm Credit Administration. These member institutions perform distinct functions. The major classes of Farm Credit System institutions are: Farm Credit Banks which provide financing to the Farm Credit System associations in their geographic regions; Production Credit Associations which provide short- and intermediate-term operating loans to their agricultural borrowers; Federal Land Bank Associations (also known as Federal Land Credit Associations) which provide long-term real estate mortgage loans to their agricultural borrowers; Banks for Cooperatives (now consolidated into a single institution called CoBank, ACB) which provide financing to their agricultural cooperative borrowers; and Agricultural Credit Associations which provide both long-term real estate mortgage loans and short- and intermediate-term operating loans to their agricultural borrowers.

Each class of institution making up the Farm Credit System has only those powers and obligations granted or imposed by Congress. The Farm Credit Banks are governed by Subchapter I of the Farm Credit Act. 12 U.S.C.

§§ 2011-2023. These sections specify, among other things, the formation, chartering, general corporate powers, capitalization, lending authority, interest rates and charges, eligible borrowers, loan terms, permissible uses of credit and the taxation of the Farm Credit Banks. The Production Credit Associations are governed by Part A of Subchapter II of the Farm Credit Act. 12 U.S.C. §§ 2071-2077. The Federal Land Bank Associations are governed by Part B of Subchapter II of the Farm Credit Act. 12 U.S.C. §§ 2091-2098. The Banks for Cooperatives are governed by Subchapter III of the Farm Credit Act. 12 U.S.C. §§ 2121-2149a.

Agricultural Credit Associations are unique among the major classes of institutions making up the Farm Credit System because their powers and obligations are not separately delineated in the Farm Credit Act. The Agricultural Credit Associations are governed solely by 12 U.S.C. § 2279c-1 which provides that they shall succeed to all powers and be subject to all of the obligations of their predecessor Federal Land Bank Associations and Production Credit Associations. While formation of the Agricultural Credit Associations is authorized by Section 2279c-1, their organization and operation are governed, i.e. their powers and obligations are defined, solely by reference to the sections of the Farm Credit Act dealing with their predecessor associations. The Agricultural Credit Associations can function only under the auspices of these incorporated sections of the Farm Credit Act applicable to the Federal Land Bank Associations and Production Credit Associations. The Farm Credit Act's

structure leads naturally to the conclusion that the taxation provisions applicable to Federal Land Bank Associations, 12 U.S.C. § 2098, apply equally to the long-term lending activities of Agricultural Credit Associations, and the taxation provisions applicable to Production Credit Associations, 12 U.S.C. § 2077, apply equally to the short- and intermediate-term lending activities of Agricultural Credit Associations.

The text of Section 2279c-1 also supports the conclusion that Congress exempted Agricultural Credit Associations from state taxation on their income from long-term real estate mortgage loans. The Agricultural Credit Associations succeed to "all powers granted under this chapter" and assume "all of the obligations imposed under this chapter" on their predecessor associations. They have no powers not granted by Congress to the Federal Land Bank Associations and Production Credit Associations under the Farm Credit Act. They assume no obligations not imposed by Congress on their predecessor associations under the Farm Credit Act.

The Ohio Supreme Court acknowledged that the term "obligations" refers to the "debts, contractually and otherwise acquired duties that the predecessor entities have undertaken." Pet. App. 6. Congress prohibits states from imposing state income tax obligations on the Federal Land Bank Associations' long-term real estate mortgage loan income. Thus, the Federal Land Bank Associations had no obligation or "duty" to pay state income tax on their income from long-term real estate mortgage lending. To permit taxation of the income of

Agricultural Credit Associations from their continuation of this lending activity would be a new obligation or "duty" – one not imposed by Congress.

Further confirmation that Agricultural Credit Associations succeed to the statutory tax immunity of Federal Land Bank Associations is found in the application of Section 2279c-1 to the merger of two or more Federal Land Bank Associations. Section 2279c-1 applies not only to mergers which create Agricultural Credit Associations. It also authorizes, and is the only section in the Farm Credit Act which does, the merger of two or more Federal Land Bank Associations. 12 U.S.C. § 2279c-1(a).[4] Unless Section 2279c-1 is read to grant state income tax immunity to the new association created by the merger of two Federal Land Bank Associations, the anomalous result would be a new association shorn of its predecessor Federal Land Bank Associations' state income tax immunity.

The interpretation of the 1987 Act adopted by the Ohio Supreme Court is also inconsistent with Congress' seventy year old policy of prohibiting states from taxing the income of Farm Credit System institutions making long-term real estate mortgage loans. The Farm Credit System was first authorized to provide long-term real estate mortgage loans in 1916. Federal Farm Loan Act, Pub. L. No. 158 § 26, 39 Stat. 360, 380 (1916). Since that

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[4] Section 2279c-1(a) provides: "Two or more associations within the same district, whether or not organized under the same subchapter of this chapter, may merge . . . "

time, each of the Farm Credit System institutions providing long-term real estate mortgage loans, whether a Federal Land Bank, 12 U.S.C. § 2055 (1986), a Farm Credit Bank, 12 U.S.C. § 2023, or a Federal Land Bank Association, 12 U.S.C. § 2098, has been exempt from state income taxation on such lending. The Ohio Supreme Court interpreted Section 2279c-1 as abandoning this policy. Congress gave absolutely no indication that it intended such a change.

In *Director of Revenue of Missouri v. CoBank ACB*, 531 U.S. 316, 121 S. Ct. 941 (2001), this Court considered whether Congress had silently changed the fifty year history of state taxation of Banks for Cooperatives, which are also members of the Farm Credit System. 531 U.S. at ___, 121 S. Ct. at 945. The Court refused to find such a change in policy absent a clear congressional statement to that effect. 531 U.S. at ___, 121 S. Ct. at 945, 946. The principle on which the Court relied in *CoBank* is equally applicable in this case. In the absence of evidence that Congress enacted a change in policy, Section 2279c-1 should be construed as continuing Congress' longstanding policy of prohibiting states from taxing Farm Credit System institutions' income from long-term real estate mortgage loans.

Finally, Section 2279c-1 cannot be construed in a vacuum. It must be construed in context and in light of the purposes of the Agricultural Credit Act of 1987. *Haggar Co. v. Helvering*, 308 U.S. 389, 396 (1940). The goal of the 1987 Act was to save the Farm Credit System and reduce the cost of credit to the System's agricultural borrowers. Congress authorized the creation of Agricultural Credit Associations in furtherance of this goal. A construction of

Section 2279c-1 which permits states to impose a new state income tax burden on the association's income from long-term real estate mortgage lending hinders the goals of the 1987 Act because it would drive up costs and the rates charged to borrowers. Such a construction should be rejected.

CONCLUSION

The Petition for a Writ of Certiorari should be granted.

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OHIO SUPREME COURT

Farm Credit Services of Mid-America, Appellant and Cross-Appellee, v. Tracy [Zaino], Tax Commr., Appellee and Cross-Appellant.

[Cite as Farm Credit Serv. of Mid-America v. Zaino (2001), 91 Ohio St.3d 564.]

Taxation – Franchise tax – Agricultural credit association that is the product of the merger of several federal land banks and a production credit association is not exempt from Ohio franchise tax.

(No. 00-505 – Submitted March 14, 2001 – Decided June 6, 2001.)

Appeal and Cross-Appeal from the Board of Tax Appeals, Nos. 97-T-889 and 98-T-333.

Per Curiam. On March 31, 1989, the Federal Land Bank Association of the Fourth District, Louisville, Kentucky, the Production Credit Association of the Fourth District, Louisville, Kentucky, the Federal Land Bank Association of Bellefontaine, Ohio, and the Federal Land Bank Association of Minerva in Warren, Ohio, merged to form appellant and cross-appellee Farm Credit Services of Mid-America, an Agricultural Credit Association, appellant, with headquarters in Louisville, Kentucky. Farm Credit Services took over the long-term loans of the merged federal land bank associations and the short-term and intermediate-term loans of the merged production credit association.

The stock issued by the merging entities converted to stock representing ownership in Farm Credit Services.

Farm Credit Services may issue further stock to investors and borrowers, borrowers must be farmers, ranchers, and producers or harvesters of aquatic products. Federal land bank associations and production credit associations have received federal instrumentality designation under federal statute. Sections 2091 and 2077, Title 12, U.S. Code. Farm Credit Services, an agricultural credit association, received designation as a federally chartered instrumentality from the Farm Credit Administration, a federal agency.

Farm Credit Services paid Ohio franchise tax for tax years 1990 through 1996. It applied for a refund for tax years 1990 through 1993, totaling $2,060,332, with the Tax Commissioner, appellee and cross-appellant, claiming immunity from state taxation under the federal Supremacy Clause. It also applied for refunds for tax years 1994 through 1996, totaling $2,733,340, by separate applications that presented the same claim. The commissioner dismissed the refund claim for tax year 1994 as untimely filed and denied the remaining refund applications. On appeal, the Board of Tax Appeals, finding that it had no jurisdiction to interpret and apply the federal Supremacy Clause, affirmed the commissioner's order.

This cause is now before the court upon an appeal and cross-appeal as of right.

Less than ten years ago, in *NLO, Inc. v. Limbach* (1993), 66 Ohio St.3d 389, 394, 613 N.E.2d 193, 197, we observed, "the federal Supremacy Clause, Clause 2, Article VI, United States Constitution, prevents the state from taxing the federal government and its instrumentalities." This year, in *Dir. of Revenue of Missouri v. CoBank ACB*

(2001), 531 U.S. 316, 121 S.Ct. 941, 148 L.Ed.2d 830, the United States Supreme Court reviewed the Supremacy Clause in a context similar to the instant case.

In *CoBank*, the court identified two types of immunity under the Supremacy Clause – explicit immunity, where Congress has expressly stated that a federal instrumentality is not subject to a state tax, and implied immunity, where Congress has not set forth any such immunity. In *CoBank*, the court held that the income of a bank for cooperatives, which has a tax status similar to production credit associations, one of the merging entities in this case, was taxable. This was so, according to the court, because "Congress has provided that banks for cooperatives are subject to state taxation." *Id.*, 531 U.S. at ___, 121 S.Ct. at 944, 148 L.Ed.2d at 835.

Federal land bank associations and production credit associations, the merging predecessors in this case, are "federally chartered insrumentalit[ies] of the United States" under Sections 2091 and 2071, Title 12, U.S. Code. Federal land bank associations are exempt from state taxes under Section 2098, Title 12, U.S. Code. Production credit associations, however, are not exempt from state taxes; according to Section 2077, Title 12, U.S. Code, only their notes, debentures, and other obligations are exempt. Thus, federal land bank associations were exempt from Ohio's franchise tax during the disputed tax years; production credit associations were not.

In section 2279c-1, Title 12, U.S. Code, Congress authorized federal land bank associations and production credit associations within the same district to merge if approved, *inter alia*, by the Farm Credit Administration

Board, a federal agency. Under this statute, the merged association possesses all powers and succeeds to all obligations of the merging associations. Finally, division (b)(2) of the statute empowers the Farm Credit Administration to "issue regulations that establish the manner in which the powers and obligations of the associations that form the merged association are consolidated and, to the extent necessary, reconciled in the merged association."

These statutes do not declare the merged association to be a federal instrumentality, and they do not provide immunity or exemption from state taxation to the merged association. Nevertheless, the Farm Credit Administration calls these merged associations "agricultural credit association[s]" and issued a charter to Farm Credit Services naming it a "Federally chartered instrumentality." Farm Credit Services relies on this charter to claim exemption from franchise tax. But the commissioner argues that the Farm Credit Administration cannot immunize an agricultural credit association from state taxation by calling it, without congressional authority, a federally chartered instrumentality.

Congress has exempted federal land banks from Ohio's franchise tax but has not exempted production credit associations. We have, however, neither of these entities before us; we have an agricultural credit association ("ACA"), the product of the merger of several federal land banks and a production credit association. Congress has not expressed an immunity from taxation for an ACA. Under *CoBank*, therefore, we must decide whether Farm Credit Services has an implied immunity from the franchise tax.

We discussed implied immunity under the Supremacy Clause in *NLO, Inc.*

"*In United States v. New Mexico, supra,* [1982], 455 U.S. [720] at 735, 102 S.Ct. [1373] at 1383, 71 L.Ed.2d [580] at 592, the court concluded that a state cannot levy a tax 'on the United States itself, or on an agency or instrumentality so closely connected to the Government that the two cannot realistically be viewed as separate entities, at least insofar as the activity being taxed is concerned.' " 66 Ohio St.3d at 394, 613 N.E.2d at 197.

In *New Mexico,* the United States Supreme Court reviewed that "much litigated and often confused field" of Supremacy Clause rulings. *United States v. Detroit* (1958), 355 U.S. 466, 473, 78 S.Ct. 474, 478, 2 L.Ed.2d 424, 429. According to the *New Mexico* court, the language quoted in *NLO,* Inc. sets forth the latitude each form of government needs in maintaining sovereignty. A private taxpayer, moreover, must stand in the shoes of the federal government to be immune. Quoting from *United States v. Detroit,* the *New Mexico* court explained that the language "[c]omports with the principal purpose of the immunity doctrine, that of forestalling 'clashing sovereignty,' *McCulloch v. Maryland* [1819], 4 Wheat. [316], at 430, 4 L.Ed. 579, by preventing the States from laying demands directly on the Federal Government. * * * At the same time, a narrow approach to governmental tax immunity accords with competing constitutional imperatives, by giving full range to each sovereign's taxing authority. * * * "

"Thus, a finding of constitutional tax immunity requires something more than the invocation of traditional agency notions: to resist the State's taxing power, a private taxpayer must actually 'stand in the Government's shoes.' " 455 U.S. at 735-736, 102 S.Ct. at 1383, 71 L.Ed.2d at 592-593.

We conclude that Farm Credit Services, as an ACA, is a privately owned business benefiting private interests. Private shareholders own the association, and private borrowers benefit from the loans that the association distributes. Farm Credit Services is a commercial enterprise that performs no governmental duty. It does not stand in the federal government's shoes and, thus, is not "so closely connected to the Government that the two cannot realistically be viewed as separate entities, at least insofar as the activity being taxes is concerned." *Id.* at 735, 102 S.Ct. at 1383, 71 L.Ed.2d at 592. Ohio can, consequently, impose the franchise tax on it.

We also dismiss Farm Credit Services' argument that language in the statute, asserting that merged associations possess all powers and assume all obligations of the merging associations, passes tax immunity to the successor association. According to normal usage, "powers" refers to the activities and actions the predecessor entities may undertake, and "obligations" refers to the debts, contractually and otherwise acquired duties that the predecessor entities have undertaken. Black's Law Dictionary (7 Ed.Rev. 1999) 1189-1190, 1102-1103.

Taxation is the rule, exemption the exception. *Vought Industries, Inc. v. Tracy* (1995), 72 Ohio St.3d 261, 264, 648 N.E.2d 1364, 1366. As Justice Thomas, writing for the

majority, observed in *CoBank*, Congress knows how to exempt federal instrumentalities from taxation. 531 U.S. at ___, 121 S.Ct. at 946, 148 L.Ed.2d at 837. If Congress does not explicitly do so, the Supremacy Clause does not supply an implicit exemption to a privately owned entity that lends funds to private individuals.

Accordingly, we agree with the commissioner's denial of the request for refunds and affirm the BTA's decision.

Decision affirmed

MOYER, C.J., DOUGLAS, RESNICK, F.E. SWEENEY, PFEIFER, COOK and LUNDBERG STRATTON, JJ., concur.

McDermott, Will & Emery, John A. Biek, Richard A. Hanson and *Theodore R. Bots*, for appellant and cross-appellee.

Betty D. Montgomery, Attorney General, and *Robert C. Maier*, Assistant Attorney General, for appellee and cross-appellant.

OHIO BOARD OF TAX APPEALS

Farm Credit Services of Mid-America, an Agricultural Credit Association, Appellant, vs. Roger W. Tracy, Tax Commissioner of Ohio, Appellee.	CASE NOS. 97-T-889 98-T-333 (FRANCHISE TAX) DECISION AND ORDER

APPEARANCES:

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ENTERED: FEB 18, 2000

Mr. Johnson, Ms. Jackson, and Mr. Manoranjan concur.

This matter is before the Board of Tax Appeals pursuant to two notices of appeal filed by appellant, Farm Credit Services of Mid-America ("Farm Credit"), from four final determinations of the Tax Commissioner. BTA

No. 97-T-889 concerns one determination issued by the Tax Commissioner, wherein the Commissioner denied Farm Credit's application for a refund of $2,060,332 in Ohio franchise tax paid for tax years 1990, 1991, 1992, and 1993. BTA No. 98-T-333 consists of three separate determinations of the Tax Commissioner addressing Farm Credit's application for a refund of $2,933,951 in Ohio franchise tax paid for tax years 1994, 1995, and 1996. The Commission denied the applications for 1995 and 1996. For 1994, the Commissioner determined that he was without jurisdiction to consider Farm Credit's application.

The Board of Tax Appeals now considers this matter upon the notices of appeal filed by Farm Credit pursuant to R.C. 5717.02, the statutory transcripts certified to this Board by the Tax Commissioner, the stipulations of the parties, and the briefs submitted thereby. The parties waived their opportunity to present additional evidence at a merit hearing before the Board.

Farm Credit challenges the Commissioner's final determinations on the ground that it is an entity exempted from state taxation under the constitutional doctrine of intergovernmental tax immunity. Specifically, Farm Credit argues that it is a federal instrumentality and that, as such, it is entitled to immunity from state taxation in the absence of an express congressional waiver. The Commissioner counters that Farm Credit may not be considered to be an instrumentality of the federal government. Moreover, the Commissioner contends that designation as an instrumentality does not automatically confer immunity from state taxation to an entity where Congress has not expressed such intent. The issues presented to this Board are therefore whether (a) Farm

Credit is a federal instrumentality and, (b) if so, is it immune from Ohio's franchise tax.

The errors raised by Farm Credit are directed toward constitutional doctrines, including the interpretation and application of the "Supremacy Clause" of Article VI, clause 2, of the United States Constitution. Farm Credit does not allege that any statutory immunity is provided by the Ohio Revised Code. In *MCI Telecommunications Corp. v. Limbach* (1994), 68 Ohio St.3d 195, the Supreme Court of Ohio addressed the role of the Board of Tax Appeals when a constitutional challenge is raised:

> "The BTA understood its role to be a receiver of evidence for constitutional challenges. Accordingly, it did so, giving the parties wide latitude in presenting the evidence. The BTA determined no facts on the constitutional questions. The commission, however, in her Proposition of Law No. IV, contends that the BTA not only receives evidence in this type of case, but must weigh the evidence and determine the facts necessary for the court's review of the constitutional questions. Since the BTA did not make findings of fact, the commissioner asserts that we should remand the case for the BTA to comply.
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> "In *Cleveland Gear Co. v. Limbach* (1988), 35 Ohio St. 3d 229, * * * paragraph three of the syllabus, we held:
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> " 'The question of whether a tax statute is unconstitutional when applied to a particular state of facts must be raised in the notice of appeal to the Board of Tax Appeals, and the Board of Tax Appeals must receive evidence concerning this question if presented, even though the Board of Tax Appeals may not

declare the statute unconstitutional. (*Bd. of Edn. of South-Western City Schools v. Kinney* [1986], 24 Ohio St.3d 184, * * * construed.)'

"We explained the process, 35 Ohio St.3d at 232 * * * :

" 'When a statute is challenged on the basis, that it is unconstitutional in its application, this court needs a record, and the proponent of the constitutionality of the statute needs notice and an opportunity to offer testimony supporting his or her view.

" 'To accommodate this court's need for extrinsic facts and to provide a forum where such evidence may be received and all parties are apprised of the undertaking, it is reasonable that the BTA be that forum. The BTA is statutorily created to receive evidence in its role as factfinder.'

"Under *Cleveland Gear*, the BTA need only receive evidence for us to make the constitutional finding. This is because the BTA accepts facts but cannot rule on the question. On the other hand, we can decide the constitutional questions but have a limited ability to receive evidence. Thus, the BTA receives evidence at its hearing, but we determine the facts necessary to resolve the constitutional question." *Id.* at 197-198. (Parallel citations omitted.)

See, also, *Valvoline Instant Oil Change, Inc. v. Tracy* (1997), 78 Ohio St.3d 53; *NACCO Industries v. Tracy* (June 7, 1996), BTA No. 95-K-1210, unreported, affirmed on other grounds (1997), 79 Ohio St.3d 314.

We have afforded both parties the opportunity to present evidence and to raise arguments regarding the

contentions specified in the notices of appeal; however, consideration of the issues lies beyond the scope of this Board's jurisdiction. Consequently, it is the decision and order of the Board of Tax Appeals that the specifications of error be overruled and that the Commissioner's final determinations be, and the same hereby are, affirmed.

I hereby certify the foregoing to be a true and complete copy of the action taken by the Board of Tax Appeals of the State of Ohio and entered upon its journal this day, with respect to the captioned matter.

/s/ Julia M. Snow
Julia M. Snow, Board Secretary

12 U.S.C. § 2077. Taxation

Each Production Credit Association and its obligations are instrumentalities of the United States and as such any and all notes, debentures, and other obligations issued by such associations shall be exempt, both as to principal and interest, from all taxation (except surtaxes, estate, inheritance, and gift taxes) now or hereafter imposed by the United States or any State, territorial, or local taxing authority, except that interest on such obligations shall be subject to Federal income taxation in the hands of the holder.

12 U.S.C. § 2098. Taxation

Each Federal Land Bank Association and the capital, reserves, and surplus thereof, and the income derived therefrom, shall be exempt from Federal, State, municipal, and local taxation, except taxes on real estate held by a Federal Land Bank Association to the same extent, according to its value, as other similar property held by other persons is taxed. The mortgages held by the Federal Land Bank Associations and the notes, bonds, debentures, and other obligations issued by the associations shall be considered and held to be instrumentalities of the United States and, as such, they and the income therefrom shall be exempt from all Federal, State, municipal, and local taxation, other than Federal income tax liability of the holder thereof under the Public Debt Act of 1941 (31 (U.S.C. 3124).

12 U.S.C. § 2279c-1. Merger of Associations

(a) In general

Two or more associations within the same district, whether or not organized under the same subchapter of this chapter, may merge into a single entity (hereinafter in this subchapter referred to as a "merged association") if the plan of merger is approved by –

(1) the Farm Credit Administration Board;

(2) the boards of directors of the associations;

(3) a majority of the shareholders of each association voting, in person or by proxy, at a duly authorized stockholders' meeting; and

(4) the Farm Credit Bank.

(b) Powers, obligations, and consolidation

(1) Powers and obligations

Except as otherwise provided by this subchapter, a merged association shall –

(A) possess all powers granted under this chapter to the associations forming the merged association; and

(B) be subject to all of the obligations imposed under this chapter on the associations forming the merged association.

(2) Consolidation

The Farm Credit Administration shall issue regulations that establish the manner in which the powers and obligations of the associations

that form the merged association are consolidated and, to the extent necessary, reconciled in the merged association.

(c) Stock issuance

(1) Plan of merger

Subject to section 2154a of this title, the number of shares of capital stock issued by a merged association to the stockholders of any association forming such merged association, and the rights and privileges of such shares (including voting power, preferences on liquidation, and the right to dividends), shall be determined by the plan of merger adopted by the merged associations.

(2) Capitalization

In accordance with section 2154a of this title, each merged association shall provide, through bylaws and subject to Farm Credit Administration regulations, for the capitalization of the association and the manner in which association stock shall be issued, held, transferred, and retired, and association earnings shall be distributed.

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IN THE

SUPREME COURT OF INDIANA

INDIANA DEPARTMENT OF STATE REVENUE, Appellant, v. FARM CREDIT SERVICES OF MID-AMERICA, ACA, Appellee.	Cause No. 49S10-9908-TA-453

APPEAL FROM THE INDIANA TAX COURT
The Honorable Thomas G. Fisher, Judge
Cause No. 49T10-9801-TA-5

September 1, 2000

SHEPARD, Chief Justice.

Farm Credit Services of Mid-America (Mid-America), an Agricultural Credit Association, claims it is exempt

from Indiana's Financial Institutions Tax under constitutional principles of intergovernmental tax immunity. We conclude it is only partially exempt.

Facts and Procedural History

Mid-America is part of the Farm Credit System, a nationwide network of cooperative, borrower-owned banks and lending institutions that were established to provide affordable credit to farmers and ranchers. 12 U.S.C.A. § 2001 (West 1989).[1]

The system includes twelve Farm Credit Banks (FCBs), located in each of twelve districts. Through local associations, these banks provide real estate loans secured by mortgages. The local associations include Federal Land Bank Associations (FLBAs), which provide long-term loans, and Production Credit Associations (PCAs) which provide short-term and intermediate loans.

Congress created the Farm Credit System in 1916 and has reformed it several times during the intervening decades. In the early 1980s, the system began to falter under unfavorable economic conditions that threatened

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[1] It is declared to be the policy of the Congress, recognizing that a prosperous, productive agriculture is essential to a free nation and recognizing the growing need for credit in rural areas, that the farmer-owned cooperative Farm Credit System be designed to accomplish the objective of improving the income and well-being of American farmers and ranchers by furnishing sound, adequate, and constructive credit and closely related services to them, their cooperatives, and to selected farm-related businesses necessary for efficient farm operations. 12 U.S.C.A. § 2001(a) (West 1989).

the stability of its lending institutions. Congress responded by enacting the Agricultural Credit Act of 1987. The Act authorized voluntary mergers between PCAs and FLBAs in an effort to streamline the structure of the lending bodies. The institution resulting from such a merger is called an Agricultural Credit Association (ACA).

Mid-America was created in 1989 through the merger of two PCAs and two FLBAs. This case arose in March 1997, when Mid-America filed an amended tax return with the Indiana Department of Revenue requesting a refund of the Financial Institutions Tax[2] it had paid for the tax years 1993 and 1994. Mid-America asserted that as a federal instrumentality it was immune from state taxation. The Department denied Mid-America's claim. Mid-America appealed to the Indiana Tax Court, where it prevailed on summary judgment. *Farm Credit Serv. Of Mid-America v. Department of State Revenue*, 705 N.E.2d 1089 (Ind. Tax Ct. 1999).[3]

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[2] Ind. Code Ann. § 6-5.5-2-1(a) (West 2000).

[3] Mid-America and the Department earlier litigated Mid-America's liability for the Indiana Gross Income Tax for 1989 and the Indiana Financial Institutions Tax for 1990 through 1992. *See Farm Credit Serv. of Mid-America v. Department of State Revenue*, 677 N.E.2d 645 (Ind. Tax Ct. 1997), *review denied*. In that case, the Department conceded that if Mid-America was found to be a federal instrumentality it was immune from taxation and entitled to a refund of taxes paid. The Tax Court determined that Mid-America was a federal instrumentality, and Mid-America thus prevailed. *Id.* at 651. Here, the Department concedes that Mid-America is a federal instrumentality, but asserts that this is not dispositive of state tax immunity.

Early Tax Immunity Doctrine

The doctrine of intergovernmental tax immunity derives from *M'Culloch v. Maryland*, 17 U.S. (4 Wheat.) 316 (1819), the landmark case holding that the State of Maryland could not impose a tax on the Bank of the United States. Chief Justice Marshall's opinion for the Court relied both on the discriminatory nature of the tax and on general principles of federal supremacy. Specifically, Marshall determined that, because the Bank was a "federal instrument" used to carry out the government's powers, state taxation would unconstitutionally interfere with the exercise of these powers. *Id.* at 425-37. Marshall explained that the individual states:

> have no power, by taxation or otherwise, to retard, impede, burden, or in any manner control the operations of the constitutional laws enacted by congress to carry into execution the powers vested in the general government.

Id. at 436.

This principle was applied broadly for many years thereafter to bar taxation by one sovereign on another, or even on the employees of another. *Davis v. Michigan Dep't of Treasury*, 489 U.S. 803 (1989); *see also, e.g., Collector v. Day*, 78 U.S. (11 Wall.) 113 (1871) (invalidating federal income tax on salary of state judge); *Dobbins v. Comm'rs of Erie County*, 41 U.S. (16 Pet.) 435 (1842) (invalidating state tax on a federal officer). In the late 1930s, however, the Court began to narrow its view of tax immunity. In *Graves v. New York ex rel. O'Keefe*, 306 U.S. 466 (1939), the Court overruled the *Dobbins-Day* line of cases and held that intergovernmental tax immunity bars only those taxes

imposed directly on one sovereign by another, or that discriminate against the sovereign to which they apply. *Id.* at 481-87. In restraining the scope of tax immunity, the Court explained:

> [T]he implied immunity of one government and its agencies from taxation by the other should, as a principle of constitutional construction, be narrowly restricted. For the expansion of the immunity of the one government correspondingly curtails the sovereign power of the other to tax, and where that immunity is invoked by the private citizen it tends to operate for his benefit at the expense of the taxing government and without corresponding benefit to the government in whose name the immunity is claimed.

Id. at 483.

Over the intervening years, the doctrine of intergovernmental tax immunity has become, in the Court's words, "a 'much litigated and often confused field,' one that has been marked from the beginning by inconsistent decisions and excessively delicate distinctions." *United States v. New Mexico*, 455 U.S. 720, 730 (1982) (internal citations omitted).

Here, both parties agree that ACAs are "federal instrumentalities", but disagree about the tax implications of this status.

Both parties urge distinct views of tax immunity. Mid-America argues that federal instrumentalities are immune from state taxation unless Congress expressly waives such immunity, while the Department argues that federal instrumentalities are subject to state taxation

unless Congress expressly exempts the instrumentality from taxation.

The Department's View

In asserting that ACAs are subject to state taxation absent a congressional statement otherwise, the Department directs us to *Arkansas v. Farm Credit Serv. of Cent. Arkansas*, 520 U.S. 821 (1997). In that case, four PCAs brought suit in U.S. District Court claiming an exemption from Arkansas sales and income taxes. The District Court granted the PCAs' motion for summary judgment, and the Court of Appeals for the Eighth Circuit affirmed. *Farm Credit Serv. of Cent. Arkansas v. Arkansas*, 76 F.3d 961 (8th Cir. 1996).

The Supreme, Court reversed on jurisdictional grounds, holding that, under the Tax Injunction Act, 28 U.S.C. § 1341, PCAs cannot sue in federal court for an injunction against state taxation unless the United States is a co-plaintiff. *Arkansas v. Farm Credit*, 520 U.S. at 831-32. In so holding, the Court considered the long-standing power of the federal government to sue to protect itself or its instrumentalities from state taxation. The Court ultimately determined that, although PCAs are congressionally designated federal instrumentalities, this designation "does not in and of itself entitle an entity to the same

exemption the United States has under the Tax Injunction Act." *Id.* at 832.[4]

The Department urges us to rely on *Arkansas v. Farm Credit* for the proposition that status as a federal instrumentality does not necessarily confer upon an entity the same rights and privileges enjoyed by the United States itself. Further, it directs us to the Court's description of PCAs:

> Whatever may be the rule under the Tax Injunction Act where a federal agency or body with substantial regulatory authority brings suit, PCA's [sic] are not entities of that description.

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[4] In representing the United States as Amicus Curiae, the Solicitor General took the position that PCAs are subject to state taxation. In so asserting, he stated:

> It would be particularly implausible to read [12 U.S.C.] Section 2077 so as to ascribe to Congress an intent to grant a production credit association a comprehensive immunity from taxation without regard to whether the federal government owned stock in it – an immunity that the associations never have enjoyed.

(App. to Appellant's Br., Br. for the United States as Amicus Curiae, at 16.)

Conversely, in *M'Culloch v. Maryland*, the Attorney General of the United States argued that the Bank of the United States was immune from state taxation, stating:

> [T]he bank, as ordained by Congress, is an instrument to carry into execution its specified powers; and in order to enable this instrument to operate effectually, it must be under the direction of a single head. It cannot be interfered with, or controlled in any manner, by the states, . . .

M'Culloch v. Maryland, 17 U.S. (4 Wheat.) at 361.

> PCA's are not granted the right to exercise government regulatory authority but rather serve specific commercial and economic purposes long associated with various corporations chartered by the United States.
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> . . . .
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> The PCAs' business is making commercial loans, and all their stock is owned by private entities. Their interests are not coterminous with those of the Government any more than most commercial interests. Despite their formal and undoubted designation as instrumentalities of the United States, and despite their entitlement to those tax immunities accorded by the explicit statutory mandate, that instrumentality status does not in and of itself entitle an entity to the same exemption the United States has under the Tax Injunction Act.

Id. at 831-32.

Mid-America's View

The decision in *Arkansas v. Farm Credit*, of course, meant that only state supreme courts and the U.S. Supreme Court possess jurisdiction to decide whether PCAs are exempt from state taxation, and Mid-America directs our attention to some cases subsequently decided by other state high courts.

In *Arkansas v. Farm Credit Serv. of Cent. Arkansas*, 994 S.W.2d 453 (Ark. 1999), *cert. denied*, 120 S. Ct. 1530 (2000), the Arkansas Supreme Court held that PCAs are exempt

from state sales and income taxes.[5] In so holding, the court reasoned that federal instrumentalities are immune from state taxation unless Congress expressly waives the immunity. *Id.* at 455. This reasoning was based on the court's interpretation of *M'Culloch* and its progeny, including the 1997 decision of the Indiana Tax Court. *See id.*

Similarly, in *Production Credit Ass'n v. Director of Revenue*, 10 S.W.3d 142 (Mo. 2000) (en banc), *cert. granted in part*, 120 S. Ct. 2716 (June 26, 2000), the Missouri Supreme Court concluded that PCAs were immune from Missouri state income taxes. The court reasoned that entities designated as "federal instrumentalities" are immune unless Congress explicitly waives immunity. The Missouri court examined the current version of the federal statute governing PCAs, noted it was silent on the matter of taxation, and concluded its inquiry, thus holding against the state. *Id.* at 143.[6]

While the cases offered by Mid-America and the Department provide an excellent background into our inquiry, we note that none of the cases are directly on point as all of the cited cases deal with PCAs rather than ACAs. While this difference is not dispositive, for reasons that will become apparent, these cases offer a view of tax

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[5] The PCAs involved were the same four PCAs in *Arkansas v. Farm Credit*, 520 U.S. 821. After the Supreme Court reversed on jurisdictional grounds, the litigants found their way to the courts of Arkansas.

[6] This is roughly how the Louisiana Court of Appeals handled the same question. *Northwest Louisiana Production Credit Ass'n v. Louisiana*, 746 So.2d 280 (La. Ct. App. 1999).

immunity doctrine that is no longer reflected in recent Supreme Court decisions.

Current Tax Immunity Doctrine

Mid-America cites *United States v. County of Allegheny*, 322 U.S. 174 (1944),[7] and several federal circuit decisions for the proposition that, where Congress is silent, state tax immunity of federal instrumentalities is implied. (Appellee's Br. at 6-7.) More recent Supreme Court cases suggest, however, that in determining tax status, a court must examine the nature of the instrumentality, and the activity being taxed.

The 1982 case *United States v. New Mexico*, 455 U.S. 720, addressed whether government contractors are immune from state taxation. In deciding that they are not, the Court provided an historical overview of tax immunity law and then said:

> We have concluded that the confusing nature of our precedents counsels a return to the underlying constitutional principle. The one constant here, of course, is simple enough to express: a State may not, consistent with the Supremacy Clause, . . . lay a tax "directly upon the United States."
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> . . . .
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> What the Court's cases leave room for, . . . is the conclusion that tax immunity is appropriate in only one circumstance: when the levy falls on

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[7] *United States v. County of Allegheny* was effectively overruled in 1958. *United States v. City of Detroit*, 355 U.S. 466 (1958); *United States v. County of Fresno*, 429 U.S. 452 (1977).

> the United States itself, or on an agency or instrumentality so closely connected to the Government that the two cannot realistically be viewed as separate entities, at least insofar as the activity being taxed is concerned. This view, we believe, comports with the principal purpose of the immunity doctrine, that of forestalling "clashing sovereignty," by preventing the States from laying demands directly on the Federal Government.

Id. at 733-35 (citations omitted).

Similarly, in *California State Bd. of Equalization v. Sierra Summit, Inc.*, 490 U.S. 844 (1989), the Court held that the doctrine of intergovernmental tax immunity does not bar the imposition of a state sales or use tax on a bankruptcy liquidation sale. In so holding, the Court said " '[a] court must proceed carefully when asked to recognize an exemption from state taxation that Congress has not clearly expressed,' " *Id.* at 851-52 (quoting *Rockford Life Ins. Co. v. Illinois Dep't of Revenue*, 482 U.S. 182, 191 (1987)), and reiterated that "[a]bsolute tax immunity is appropriate only when the tax is on the United States itself 'or an agency or instrumentality so closely connected to the Government that the two cannot realistically be viewed as separate entities, . . . ' " *Id.* at 849 (quoting *New Mexico*, 455 U.S. at 755); *see also United States v. California*, 507 U.S. 746, 753 (1993) (quoting *New Mexico*); *South Carolina v. Baker*, 485 U.S. 505, 523-24 (1988) (quoting *New Mexico*).

We cannot read these cases and hop directly to the conclusion that anything labeled a federal instrumentality automatically possesses immunity from state taxation.

The designation "federal instrumentality" certainly carries with it a strong possibility of such immunity, but the inquiry cannot simply end there.

After all, the last century was awash in Congressional enactments creating scores of commissions and corporations to carry out programs that the national legislature deemed important federal missions. From the Red Cross and the Boy Scouts to Amtrak and Comsat, these entities have been called by various names: federal instrumentalities, federal corporations, and government-sponsored enterprises, to mention a few.

Perusal of the field rapidly demonstrates that the name Congress chooses to give (or even not give) a particular entity does not by itself determine whether the entity is "an agency or instrumentality so closely connected to the Government that the two cannot realistically be viewed as separate entities." *New Mexico*, 455 U.S. at 735.

The statute creating the Red Cross, for example, says nothing about tax immunity and describes the corporation simply as "a body corporate and politic in the District of Columbia."[8] The Red Cross nevertheless has been deemed part of the Government for tax immunity purposes because of its close connection to federal departments and because the President appoints the board.[9] The Boy Scouts were created by Congress as a "corporation under the laws of the District of Columbia" in a statute

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[8] 36 U.S.C.A. § 1 (West 1988).

[9] *Department of Employment v. United States*, 385 U.S. 355 (1966).

that says nothing about tax immunity,[10] and the Scouts appear exempt for reasons unrelated to sovereign immunity. Comsat, formally the Communications Satellite Corporation, has a board chosen by its private shareholders, who have provided its capital; in creating Comsat, Congress declared it "will not be an agency or establishment of the United States Government."[11]

Such disavowals by Congress, however, do not bring constitutional inquiries to a close. The National Railroad Passenger Corporation, created by Congress as "a for profit corporation",[12] recently cited a similar provision in the statute ("not an agency")[13] to assert that it was not the government. Though the case arose under rather different circumstances than the ones we examine today, the Court spoke rather broadly about Amtrak's contention

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[10] 36 U.S.C.A. § 24 (West 1988).

[11] 47 U.S.C.A. § 731 (West Supp. 2000). Comsat bears some resemblance to the venture launched by Congress during an earlier technological revolution: the Union Pacific Railroad. Congress created the corporation and the President appointed two members of the board. Act of July 1, 1862, § 1, 12 Stat. 491. Though Congress was silent on the question of tax immunity, we think it unlikely that the Union Pacific was ever regarded as exempt.

[12] 45 U.S.C.A. § 541 (West 1987) (repealed 1994).

[13] In establishing the Amtrak corporation, Congress provided:

> The Corporation shall be operated and managed as a for profit corporation, the purpose of which shall be to provide intercity and commuter rail passenger service,. . . . *The Corporation will not be an agency or establishment of the United States Government.*

Id. (emphasis added).

that the language of the statute settled the matter: "[I]t is not for Congress to make the final determination of Amtrak's status as a Government entity for purposes of determining the constitutional rights of citizens affected by its actions." *Lebron v. National R.R. Passenger Corp.*, 513 U.S. 374, 392 (1995). On matters of such gravity, labels do not account for much. As the Court said in considering the finances of the Reconstruction Finance Corporation: "That the Congress chose to call it a corporation does not alter its characteristics so as to make it something other than what it actually is." *Cherry Cotton Mills, Inc. v. United States*, 327 U.S. 536, 539 (1946).

We thus proceed to examine what Mid-America "actually is."

Agricultural Credit Associations

As we mentioned above, ACAs such as Mid-America are entities created by merging FLBAs and PCAs.

FLBAs are federally chartered instrumentalities of the United States, offering long-term loans to farmers and farm-related businesses for land and other capital purchases. 12 U.S.C.A. § 2091 (West 1989); H.R. Rep. No. 100-295(I), at 55 (1987), *reprinted in* 1987 U.S.C.C.A.N. 2723, 2727.

Since their inception, FLBAs have enjoyed immunity from state taxation pursuant to the following specific exemption enacted by Congress:

> Each Federal land bank association and the capital, reserves, and surplus thereof, and the income derived therefrom, shall be exempt from

> Federal, State, municipal, and local taxation, except taxes on real estate held by a Federal land bank association. . . .

12 U.S.C.A. § 2098 (West 1989).

PCAs are also "[f]ederally chartered instrumentalit[ies] of the United States"; they are privately-owned, corporate financial institutions organized by ten or more farmers to provide short-term and intermediate loans to farmers. 12 U.S.C.A. § 2071, 2075 (West 1989). These loans are intended to cover seasonal operating expenses, land improvement, and purchases of farm equipment, livestock and buildings. H.R. Rep. No. 100-295(I), *supra*, at 55.

Unlike FLBAs, PCAs possess limited express tax immunity. First created by the Farm Credit Act of 1933, PCAs were initially funded by government loans, and were afforded immunity from state taxation as long as they were publicly-owned. The statute providing for this exemption, which remained substantially unchanged until 1985, read:

> Each production credit association and its obligations are instrumentalities of the United States and as such any and all notes, debentures, and other obligations issued by [PCAs] shall be exempt, both as to principal and interest from all taxation . . . imposed by the United States or any State, territorial, or local taxing authority. [PCAs], their property, their franchises, capital, reserves, surplus, and other funds, and their income shall be exempt from all taxation now or hereafter imposed by the United States or by

> any State, territorial, or local taxing authority; . . . except that any real and tangible personal property . . . shall be subject to Federal, State, territorial, and local taxation to the same extent as similar property is taxed. *The exemption provided in the preceding sentence shall apply only for any year or part thereof in which stock in the production credit associations is held by the Governor*[14] *of the Farm Credit Association.*

Farm Credit Act of 1971, Pub. L. No. 92-181, § 2.17, 85 Stat. 583, 602 (1972) (emphasis supplied).

During the 1950s and 1960s, stock held by the Farm Credit Association was gradually retired. By 1968, PCAs were entirely owned by their borrower-members, as they continue to be. *See* H. R. Rep. No. 92-593 (1971), *reprinted in* 1971 U.S.C.C.A.N. 2091, 2098; *Smith v. Russellville Prod. Credit Ass'n*, 777 F.2d 1544, 1550 (11th Cir. 1985).

In 1985, Congress deleted the express tax exemption that had been granted to publicly-owned PCAs. What remains in the current statute is a partial exemption:

> Each production credit association and its obligations are instrumentalities of the United States and as such any and all notes, debentures, and other obligations issued by such associations shall be exempt, both as to principal and interest, from all taxation . . . imposed by the

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[14] Before 1985, the Chairman of the Farm Credit Association was called the "Governor." 12 U.S.C.A. § 2241 (West 1989), Historical and Statutory Notes, Interim Implementation of 1985 Amendment, Pub. L. No. 99-205, § 402.

> United States or any State, territorial, or local taxing authority, . . .

12 U.S.C.A. § 2077 (West 1989).[15]

Both PCAs and FLBAs are privately owned and controlled. They are, however, considered "[g]overnment-sponsored entities" and have a preferred place in the nation's money markets, although debt issuances are not guaranteed by the United States. H.R. Rep. No. 100-295(I), *supra*, at 55. The associations are governed by boards of directors elected from and by the stockholders. *Id.*[16]

The power to merge FLBAs and PCAs is found in 12 U.S.C. § 2279c-1. While this statute authorizes such mergers, it does not establish what the tax implications are for the resulting ACA. The statute provides only that a merged association shall:

> (A) possess all powers granted under this chapter to the associations forming the merged association; and

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[15] By the time this amendment was adopted, there were no publicly-owned PCAs entitled to the exemption. *See Farm Credit Serv. of Cent. Arkansas v. Arkansas*, 76 F.3d at 967 (Loken, J., dissenting). Thus, Mid-America concludes that PCAs were subject to taxation before 1985, and not afterwards, inasmuch as taxation was no longer "expressly authorized." (*See* Appellee's Br. at 14.)

[16] As a condition of obtaining a loan, borrowers are required to purchase stock in the association in an amount equal to a set percentage of the face amount of the loan. H.R. Rep. No. 92-593, *supra*, 1971 U.S.C.C.A.N at 2097; 12 C.F.R. § 614.4335 (2000).

> (B) be subject to all of the obligations imposed under this chapter on the associations forming the merged association.

12 U.S.C.A. § 2279c-1(b)(1) (West 1989).

As discussed above, Congress enacted the Agricultural Credit Act of 1987 in response to an agricultural depression that began in the early 1980s. The 1987 Act was passed, in essence, to salvage the Farm Credit System. H.R. Rep. No. 100-295(I), *supra*. Mergers between Farm Credit entities were authorized in an effort to increase efficiency within the system while maintaining control by the farmer-shareholders. Such evidence of Congressional intent as we can find emphasizes not the close connection of the United States to lenders but the close connection of the local owners. In recommending legislation to allow such mergers, the House Committee on Agriculture said:

> The Federal Land Bank System has served as the primary lender of long-term agricultural credit since its inception in 1916. Competition from other institutions has existed but the Farm Credit System's ability to obtain funds in capital markets on Wall Street (known as agency status) has allowed the System to offer lower interest rates to farmers and ranchers.
>
> . . . .
>
> The loan portfolio of the Farm Credit System has shrunk considerably in the last five years. . . . [T]he Farm Credit Systems' [sic] seventy year-old structure must be reorganized in order that the System compete in an agricultural lending environment that is going through its

> biggest changes since farmers began borrowing money. . . .
>
> Realizing the structure was quickly becoming outmoded and incapable of maintaining a competitive position, the Committee felt the Farm Credit System must make certain changes. . . .
>
> Because the concept of a member-owned cooperative is appreciated to the highest degree at the local level, the fairest and most effective approach in dealing with the problem would be to down-size the middle layer (district banks) of the bureaucracy. This approach would allow the stockholders to continue control production credit associations and Federal land bank associations while accruing significant savings on borrower interest costs, especially in years to come.

H.R. Rep. No. 100-295(I), *supra*, at 65-66.

Legislative and regulatory history also suggests that institutions created by mergers were deemed to retain the characteristics of the former entities. The statute governing mergers of Farm Credit entities states: "The Farm Credit Administration shall issue regulations that establish the manner in which the powers and obligations of the associations that form the merged association are consolidated and, to the extent necessary, reconciled in the merged association." 12 U.S.C.A. § 2279c-1(b)(2) (West 1989).

The FCA regulations define an agricultural credit association as an "association[ ] created by the merger of one or more Federal land bank associations or Federal land credit associations and one or more production

credit associations . . . " Farm Credit Administration Definition, 12 C.F.R. § 619.9015 (2000). The regulations also define a merger as the "[c]ombining of one or more organizational entities into another similar entity," or "the combination of one or more associations into a continuing constituent association, which retains its charter and bylaws (except as amended to effect the merger proposal)." *Id.* §§ 619.9210, 611.1122 (2000).[17]

Thus, a merged association, like an ACA, is not considered a new organizational entity, but rather a combination of the two previous entities. And although PCAs and FLBAs are merged to streamline the Farm Credit System, the resulting ACA continues to provide the same services to the same constituents as the original entities.

Mid-America's own structure reflects this definition of "merger." With offices principally located in Louisville, Kentucky, Mid-America's territory also includes Indiana, Tennessee, and parts of Kentucky and Ohio. Farm Credit Service of Mid-America, ACA, *1999 Annual Report* (2000) [hereinafter Annual Report]. Mid-America consists of an ACA parent company, and two wholly-owned subsidiaries: Farm Credit Services of Mid-America, FLCA (Federal Land Credit Association),[18] and Farm Credit Services

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[17] Conversely, a consolidation is defined as the "[c]reation of one new organizational entity from two or more existing entities or parts thereof." 12 C.F.R. § 619.9110.

[18] A federal land credit association (FLCA) is an entity that has received a transfer of direct long-term lending authority from an FLBA. An FLCA is authorized to make real estate mortgage loans. Farm Credit Administration Definitions, 12 C.F.R. §§ 614.4030, 619.9155 (2000); 12 U.S.C.A. § 2279b (West 1989).

of Mid-America, PCA. The FLCA makes secured long-term agricultural real estate and rural home mortgage loans while the PCA makes short and intermediate-term loans. *Id.*[19] The entity thus performs two distinct and seemingly autonomous functions: long-term mortgage lending through an FLCA and short-term lending through a PCA.

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[19] Mid-America's Annual Report states:

> On December 1, 1999, the Association restructured its operations. Instead of the single ACA entity, the Association is now composed of an ACA parent company with two wholly-owned subsidiaries. The subsidiaries are chartered as a PCA and an FLCA. The restructuring preserves certain advantages of the ACA structure while clarifying the tax exemption of the mortgage operations by conducting those operations in a separate subsidiary chartered as an FLCA.

Annual Report, supra, Management's Discussion and Analysis, at 2.

> As discussed in Note 1, the Association moved to a parent-subsidiaries structure effective December 1, 1999. In a case of a completed restructuring using this subsidiary pattern by another ACA, the IRS issued a private letter ruling that the income of a new FLCA subsidiary is, under the Farm Credit Act, exempt from taxation.

Annual Report, supra, Notes to Consolidated Financial Statements, at 5.

> Although technical advice memoranda issued by the IRS may not be used or cited as precedent, we find the aforementioned helpful in uncovering Mid-America's understanding of the tax implications of its bifurcated structure.

Congress has been very clear in its decision that long-term lending institutions, such as FLBAs and FLCAs, should enjoy immunity from state taxation. Most writers on the general principles of intergovernmental tax immunity take for granted that Congress possesses the power to confer immunity. Thus, the FLCA or long-term mortgage lending portion of Mid-America's operations should not be factored into a calculation of taxes owed by Mid-America under Indiana's Financial Institution Tax.

With respect to the PCA or short-term lending portion of Mid-America's operations, we reach a different conclusion. Since 1985, Congress has afforded only partial tax immunity to PCAs. Before that, it protected PCAs from state taxation only while they were publicly-owned. PCAs are now entirely privately-owned and controlled. They obtain their funds in the private market and disperse them without any participation by the United States. Their farmer/shareholders choose the managers of the enterprise. In light of these characteristics of the entity and Congress's removal of the exemption, we cannot conclude that a PCA is "an agency or instrumentality so closely connected to the Government" so as to afford it an exemption from state taxation. As the Supreme Court said: "Their interests are not coterminous with those of the Government any more than most commercial interests." *Arkansas v. Farm Credit*, 520 U.S. at 831.

The Indiana Financial Institutions Tax is measured by calculating the taxpayer's adjusted gross income, or apportioned income, for the privilege of transacting the business of a financial institution in Indiana. Ind. Code Ann. § 6-5.5-2-1 (West 2000). Although Mid-America only formally divided its operations into two subsidiaries in

1999, we presume it could separate and calculate the gross income derived from long-term mortgage loans from that derived from short-term loans for the tax years 1993 and 1994.

Thus, the Department is entitled to tax that part of Mid-America's gross income derived from Mid-America's short-term PCA operations, but not the income generated by long-term FLBA lending, which enjoys immunity from state taxation under the Farm Credit Act.

Conclusion

We thereby reverse and remand to the Indiana Tax Court for proceedings to determine the tax due on Mid-America's PCA operations.

Dickson and Rucker, JJ., concur
Boehm, J., dissents with separate opinion in which Sullivan, J., joins.

BOEHM, Justice, dissenting.

I agree in large part with the majority's account of tax immunity doctrine past and present. And the majority's result is inviting. As the majority explains, PCAs enjoy only limited immunity from state and local taxation, but FLBAs enjoys complete immunity. One can imagine that an ACA, as the product of a merger of these two, might enjoy tax immunity for those activities traditionally conducted by FLBAs, but not for those historically performed by PCAs. Nonetheless, it seems clear to me that

Mid-America, as an ACA, is a new entity, albeit one formed by the merger of a PCA and an FLBA. Neither party in this lawsuit contends that ACAs enjoy partial immunity from state taxation and I cannot find a statutory basis for the majority's result that splits Mid-America's tax liability based on long-term versus short-term lending. Forced to choose between the poles of complete taxability and total immunity for ACAs, I believe taxability is more consistent, with the statutory pattern that gives rise to this question of federal law. Moreover, it seems to me that the majority's Solomonic solution will lead to endless disputes as to the character of various transactions as the creative juices of accountants, tax lawyers, and revenuers begin to flow.

The majority points out that in evaluating a claim of immunity current Supreme Court law requires us to "examine the nature of the instrumentality, and the activity being taxed." *Indiana Dep't of State Revenue v. Farm Credit Servs.*, 734 N.E.2d 551, 556 (Ind. 2000). I agree with that standard but disagree as to the result it produces. An ACA is a privately owned entity operated for the benefit of private interests. I believe this strongly suggests a taxable entity. And the nature of an ACA's activities-financing farmland acquisitions and short-term borrowings – points in the same direction. These activities are conducted by a myriad of other privately owned taxable entities. Thus, both the nature of the entity and its activities, in the interest of competitive fairness, suggest taxability, not immunity. It is of course true that all of these activities were once immune from state taxation if conducted by a PCA or an FLBA. But that was by reason of the nature of the entity and/or by express congressional

mandate, not by reason of the activity itself. I also think it is significant that we are interpreting a relatively recently enacted statute. It seems improbable to me that immunity was intended by omission in this era of legislative moves toward privatization and reliance on market forces.

Nor can I find support for immunity in the express language of the statute authorizing the merger of PCAs and FLBAs into ACAs. Congress has been deafeningly silent on the issue of state taxation of ACAs. Citing *United States v. Allegheny County*, 322 U.S. 174 (1944), Mid-America claims that in the absence of an expression of congressional opinion it is entitled to immunity as a "federal instrumentality." The Department urges that, even though some earlier cases found tax immunity despite congressional silence, the current statutes governing the Farm Credit System expressly address this subject and confer varying degrees of immunity on the several farm credit entities. *See* 12 U.S.C. §§ 2001 to 2279 (1994). The Department maintains that in the absence of an explicit conferral of immunity, we should conclude there is none.

As the Supreme Court held, status as a federal instrumentality does not confer automatic immunity under the Tax Injunction Act. *See Arkansas v. Farm Credit Servs.*, 520 U.S. 821, 831-32 (1997). And, as the majority notes, recent Supreme Court cases make clear that this status carries no talismanic defense to a state revenue agent. *See Farm Credit Servs.*, 734 N.E.2d at 556-57. These cited statutory provisions produce, at best, a standoff, and no other statutory language seems to me to bear on this issue. The majority points out that the statute specifies that the merged association will "possess all powers granted

under this chapter to the associations forming the merged association" and "be subject to all of the obligations imposed under this chapter on the associations forming the merged association." 12 U.S.C. § 2279c-1. I find neither provision relevant here. It is an odd if not distorted usage to speak of a tax immunity as either a "power" or an "obligation" of a corporate entity. One thinks of the former as referring to the activities and actions the entity may undertake, and the latter as referring to the debts, contractual and other acquired obligations, of the predecessor. Neither, in conventional usage, refers to a status such as immunity from taxes. And, as the Fourteenth Amendment witnesses, the terms to confer an immunity have long been familiar to legislators and even the drafters of constitutions, but are glaringly absent here.

In sum, in today's world, given the trends identified by the majority against implied immunity, it seems more probable to me that if Congress had intended to provide immunity for some activities of an ACA but not for others, it would have said so explicitly. Congress did something like this with respect to PCAs, whose obligations are exempt from state taxation in the hands of their holders, but whose activities are subject to state taxation. *See id.* § 2077. We thus have a statutory scheme in which two farm credit entities are explicitly exempted from all state taxation, two are explicitly partially exempt from taxation, and one – the ACA – enjoys no explicit exemptions. *See id.* §§ 2023, 2077, 2098, 2134. As the Supreme Court put it, "Where Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that

Congress acts intentionally and purposely in the disparate inclusion or exclusion." *Rodriguez v. United-States*, 480 U.S. 522, 525 (1987) (per curiam) (quoting *Russello v. United States*, 464 U.S. 16, 22-23 (1983)). If Congress had intended to exempt the newly created ACAs from state and local taxation, I believe it would have said so.

All of the foregoing applies to the tax years before 1999. Mid-America, whether for tax or other reasons, has now apparently dropped its operations into two wholly owned subsidiaries. One of these is a Federal Land Credit Association and, therefore, like an FLBA, is exempt by virtue of its status. The other is a taxable PCA. How these tax statuses affect a consolidated return, if one is required or electable, is a matter for another day. For now, the issue is solely Mid-America's pre-reorganization tax status, which I would conclude is that of a fully taxable entity like any other private enterprise. Accordingly, I respectfully dissent.

SULLIVAN, J., concurs.